

Financial Q&A with the CFO



"The Postal Service continues to build its financial strength. During 1998, we declared a dividend equivalent to \$800 million to the American public, by delaying our approved general price increase. We were able to do this because our institution's culture is changing to put an emphasis on using financial information to make decisions. Watching the bottom line is as important to us as serving you, our customers."

M. Richard Porras
Chief Financial Officer
and Senior Vice President

M. Richard Porras, the Chief Financial Officer and Senior Vice President, answers some frequently asked questions about the Postal Service.

If the Postal Service is making money, why does it need a rate increase?

Like any business, inflation drives our costs, and so does delivering mail to almost 1 million new addresses each year, not to mention the cost of processing the almost 20 billion additional pieces of mail since our last rate increase. Add that all up and you can see that we need additional revenue to cover these increased costs. While we are constantly improving our efficiency to help keep costs down, we simply cannot cover all of these additional costs without some increase in our rates. But our rate increase is only one cent, just one penny. The last time rates increased only one cent was in 1968 when the price of a First-Class stamp went from 5 to 6 cents. Not only is this the smallest percentage increase ever, but it's also less than the rate of inflation.

If the Postal Service needs more money, why doesn't it just get more from the federal government?

Because the Postal Service isn't funded by government appropriations. Our revenues come from selling our services to customers. More importantly, we haven't received any operating subsidies since 1982. Since then, we've been self-supporting, and we haven't received one penny from the American taxpayer.

Why doesn't the Postal Service's net income increase every year like the income of most companies?

Unlike most companies, we can't just raise our prices as our costs increase. Our Board of Governors has to ask an independent body—the Postal Rate Commission—to review and recommend any increase in postal rates. Only then can the Governors act on their recommendation. This entire process—from the time we begin our rate increase request until the time the increase goes into effect—can take 16 to 18 months from start to finish. And during this time our costs for things like fuel, rent, utilities, salaries and benefits keep going up, over 19 percent since our last rate increase in 1995. So our net income decreases each year until we can bring our prices more in line with our costs.

Why does the Postal Service, a government agency, have a profit?

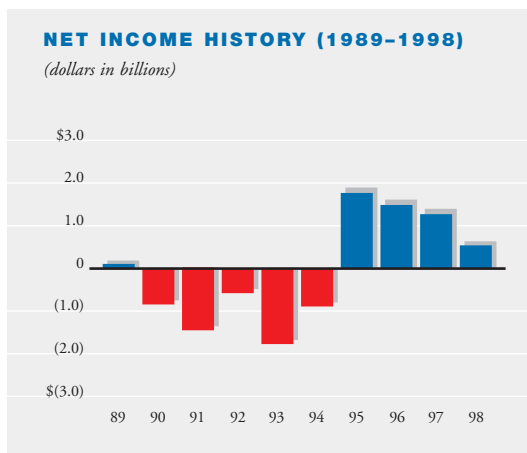
There are important reasons that explain why a government agency such as the Postal Service may need a profit or surplus just like a private business. Like a business, we need funds to make investments in new equipment and technology that allow us to make service improvements that improve customer satisfaction, upgrade our infrastructure allowing us to reduce costs, and meet the needs of a growing American population.

Since we are self-supporting, these funds (cash) must come from our operating activities, or we must borrow money. Historically, we borrowed money based on our capital plans for improvements to property and equipment. Under this policy, our debt reached almost \$10 billion. This led to higher interest payments and higher rates. Through negotiations with the U.S. Treasury's Federal Financing Bank, we were able to establish short-term lines of credit. This enabled us to minimize cash and reduce our debt. Since 1994 we have reduced our debt to \$6.4 billion. This is one of the reasons our upcoming rate increase is the lowest percentage increase in our history.

Profits, which are a component of cash from operating activities, are a necessary part of prudent cash management that allow us to make the investments we need to operate as efficiently as possible while delivering the kind of service and prices our customers want. In addition, the Board has directed us to restore our equity which was reduced by prior years' losses. These losses accumulated to almost \$9 billion between 1971 and 1994. To date we have reduced our prior year losses to under \$4 billion.

How does Economic Value Added (EVA) help the Postal Service deliver the mail?

Employees must have a reason to open their minds to change. It can be the threat of competition, reregulation, or a dramatic shift in the way they are compensated, such as bonuses. We think our EVA program is the correct way to implement change. It is considered a best business practice in the boardrooms of many major companies, such as Coca-Cola and General Electric. Our EVA program, which funds our group incentive program for management and nonbargaining employees, focuses on actual results, tying their pay to their job performance and rewarding the most efficient and productive employees. In the three years we have had our EVA program, we have seen dramatic changes in employee behavior. This program



encourages employees to work better, more efficiently, and more creatively. It creates a sense of ownership in employees so we all manage our business more efficiently, control costs, and serve our customers better by developing the products and services they want. With EVA, we can invest efficiently and effectively in the equipment and facilities that our employees need to deliver the service our customers expect.

How will the Five-Year Strategic Plan help the Postal Service comply with the new Government Performance and Results Act?

The strategic plan maps our future. It commits us to achieving excellence in customer service, practicing aggressive cost management and creating unique customer value. It defines our mission, outlines a set of goals, describes the strategies we will use to achieve those goals, and establishes the measures for how well we achieve our goals. The core of the Plan is to ensure that the Postal Service continues to deliver reliable, secure, prompt, and cost-effective service. With the Plan, we will be able to fulfill our commitment to provide the same service at the lowest possible price to all our customers, from individuals to international corporations, no matter where they're located, from the most remote outpost in Alaska to the crowded streets of the largest cities. We don't serve just the select few who can afford our services; we serve everyone everywhere at the same price. That's what we mean by universal service.

Why does the Postal Service plan for equity restoration each year?

Equity is the value of all a company's assets minus all its liabilities. Normally, companies should, at a minimum, have sufficient revenues to cover their costs and to maintain their equity. But for 23 years, from 1971 to 1994, the Postal Service took in less

than was required, building up a deficit that totaled \$9 billion, and equity seriously declined. Equity is an important representation of a company's financial health; negative equity tells you that all is not well with a company's financial condition. We're working to restore our equity by reducing expenses, raising revenues, managing our cash flow, and increasing our investments to ensure future income. We are now on the road to financial health. Since 1995, we've been restoring equity by setting our rates to include a modest surplus at a rate determined by the Board of Governors. Beginning with the 1995 rate increase, our "break even" point each year includes the money we need to restore equity over about a ten-year period.

What role does diversity play in the Postal Service's financial operations?

We embrace diversity, not just because it's the right thing to do but because it's also plain good business. For example, the Hispanic community is the fastest growing segment of the population, so we need to make an aggressive effort to serve this approximately \$250 billion consumer market. Following our strategic plan we have established multicultural marketing programs and small business centers in key cities to reach out to minority markets and businesses. We've also established programs to improve diversity at the Postal Service including one to increase our minority workforce and to increase the number of minority suppliers who do business with us. We've started our Dinero Seguro/Sure Money money transfer service so consumers have a safe, rapid and guaranteed way to send money to family and friends in Mexico. We may expand this service to several other countries including the Dominican Republic, the Philippines and El Salvador. It just makes good business sense to do all that we can to work with this market and serve it better.

We want to run the most efficient organization possible while delivering the highest customer satisfaction. Everything we do is aimed at helping us run our business more efficiently and serving our customers better. We make over 650 million deliveries each day, and we want to make sure that in delivering every piece of mail reliably, securely, and promptly, we do it as efficiently as possible.

M. Richard Porras

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Chief Financial Officer and Senior Vice President

**62,000
mail
handlers**

Every one of our 62,000 mail handlers move an average of 3.2 million pieces of mail per year.